TEXAS DEPARTMENT OF HOUSING AND COMMUNITY AFFAIRS

AUDIT COMMITTEE MEETING

John H. Reagan Building
Room JHR 140
105 W. 15th Street
Austin, Texas

July 28, 2016
8:00 a.m.

MEMBERS:

LESLIE BINGHAM ESCAREÑO, Chair
T. TOLBERT CHISUM, Member
TOM H. GANN, Member
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PROCEEDINGS

MS. BINGHAM ESCAREÑO: Good morning. Nice to see everybody. This is the Audit Committee of the Texas Department of Housing and Community Affairs. We have -- let me take roll call first.

So I'm here. So nice to have Mr. Chisum back.

MR. CHISUM: I'm here. Thank you.

MS. BINGHAM ESCAREÑO: And Mr. Gann.

MR. GANN: Here.

MS. BINGHAM ESCAREÑO: So we're all present and we can do business. We actually just have one agenda item for action; the rest of them are report items. If you gentlemen had a chance to look at the minutes, let me know if you recommend any changes. Otherwise we'll entertain a motion for approval.

MR. CHISUM: So moved.

MR. GANN: Second.

MS. BINGHAM ESCAREÑO: Okay. Mr. Chisum makes the motion; Mr. Gann seconds. All in favor aye.

(A chorus of ayes.)

MS. BINGHAM ESCAREÑO: Opposed?

(No response.)

MS. BINGHAM ESCAREÑO: Motion carries.

Good morning, Mark. So we have three report items on this morning. One of them is just a kind of
presentation and discussion of our sources and uses.

    MR. SCOTT: Yes, ma'am.

    MS. BINGHAM ESCAREÑO: Would you like to start
with that report item --

    MR. SCOTT: Yes.

    MS. BINGHAM ESCAREÑO: -- this morning?

    MR. SCOTT: The Internal Auditing Act requires
periodic audits of a state agency's financial and
accounting systems and controls. And I like to do this
overview audit, which I call sources and uses, once per
biennium to show and analyze how the Agency's money is
received and spent.

    It kind of connects the dots between various
external reports where financial information is cited.
This audit can also be used as a base for future audits.
It's the first time it has been done at TDHCA, and so with
each go around it should become more informative. I've
done these at other agencies, and the boards have always
indicated that they found the sources and uses audit to be
a good reference tool as well as an audit.

    TDHCA has a complex financial structure which
is necessary to promote a wide variety of activities. The
Agency's financial statements and the SAO opinions on
various funds are posted onto the Agency's website. Their
reports on the basic financial statements are about 104
pages long, and they're in a format that can be hard to read. They're kind of written for accountants, bankers, and other financial users.

The Internal Audit Report is for the purpose of internal analysis and information. On pages 2 and 3 of the Report I have the budget amounts that are included in the TDHCA portion of the state's appropriations bill. This is often referred to as a bill pattern.

On the LBB website, which has the state's annual budgets, the TDHCA budget is included in Article 7, Business and Economic Development. The General Appropriations Act and information available through the Legislative Budget Board uses the term "funds available" with respect to TDHCA's finances.

The GAA appropriates approximately $243 million per year to TDHCA, and the bill pattern includes a statement that the amount represents 27 percent of what is available to TDHCA. So if you gross that up, as accountants say, it may sound as if TDHCA will spend approximately $900 million per year, but that's not the case.

The note in the calculation in the GAA refers to amounts that are in the Housing Trust Fund that will be expended over a much longer period. I just wanted to point that out so someone won't think the Agency spends
four times what is appropriated.

(General laughter.)

MR. SCOTT: The actual amount of funds TDHCA spent or passed through in 2015 was approximately $312 million. It is averaged approximately $344.5 million per year over the past three years.

The Agency spent less on energy assistance in 2015 than in the prior years running out the ARRA money. Also in 2013 the Agency expended $4.2 million on Neighborhood Stabilization Program and did not have NSP expenditures in the subsequent years.

So the difference in the total Agency expenditures versus the Agency's appropriations is the money that is expended from the funds held outside the Treasury. The majority of the appropriated funds are federal funds out of what is called the Community Affairs Funds Number 127, which includes the Energy Assistance Funds.

The amount from the state's general revenue fund is about $13 million. About $19.5 million is appropriated receipts, which includes items like monitoring fees.

I'll pause for a second to see if there's any questions so far.

MS. BINGHAM ESCAREÑO: Any questions?
(No response.)

MS. BINGHAM ESCAREÑO: Thanks, Mark.

MR. SCOTT: Section B of the Audit Report --
Section B of the Internal Audit Report includes a reconciliation of the amounts referenced in the Agency's bill pattern and the information in the Agency's LAR.

The bulk of the money kept outside the state treasury is in mortgage-backed securities. The rest is in cash or cash equivalents. And again, the SAO audits those funds.

Section C of the Audit Report just describes the Housing Trust Fund is kept outside the state Treasury and placed with the Texas Treasury Safekeeping Trust Company.

Section D of the Audit Report, indirect cost and administration: The Agency's administration is funded by a direct line item in the appropriations and by charges of an indirect rate to federal agencies. The approved indirect cost rate is 44.4 percent, and the total charged to federal sources is around $1.7 million per year.

When we did the payroll audit last year, the annual salaries of TDHCA, including Manufactured Housing, were approximately $18.5 million per year. Some of the salaries are appropriately charged as direct costs to federal programs.
We tested the indirect cost allocations and they were correctly calculated. Just as a note, to directly charge staff time, et cetera, to federal sources can required a larger record-keeping burden.

Section F of the Audit Report is the Lower Income Housing Tax Credits. And a large part of the housing activities are financed by tax credits by means of which the Agency creates the multifamily housing which is so often discussed at the board meetings.

The tax credits kind of jumpstart the process. When a tax credit is awarded, the result will be the issuance of an IRS Tax Form 8609. These are used by developers to offset their tax liability. TDHCA receives some fee income to defray the administrative costs of handling the tax credit program.

Section G was on reconciliation. We cross-checked the various sources of information both internally and externally reported to make sure they either matched or could be reconciled. We had minor observations on budget information related to interagency contract with the Agriculture Department and to the payroll-related costs.

And Exhibit A just provides more detail on the Agency's goals and strategies. The information is from the LAR and the Agency's bill pattern. And that concludes
my discussion of the Sources and Uses Audit.

MS. BINGHAM ESCAREÑO: Okay. Any questions from the committee members?

MR. CHISUM: Well done.

MR. GANN: Well done.

MR. SCOTT: Thank you very much.

MS. BINGHAM ESCAREÑO: Great. So, Mark, so other than just the minor observations under reconciliations, there weren't any other really material internal findings?

MR. SCOTT: Yes, ma'am, that's correct.

MS. BINGHAM ESCAREÑO: Okay. Very good. Come on up, Tim. So I was just going to make an observation. We were sharing before the committee meeting started that when Tim and I and Mr. Oxer were talking with Mark as a candidate for the director position, one of the things that really appealed to us was the recommendation to do a Sources and Audit -- a Sources and Uses Audit.

And at the time it just sounded like a good kind of fiscally responsible thing to do. And so I don't know if this is a primary outcome or secondary outcome, but the fact that now we have this kind of well-thought-out explanation of what we have all learned, you know, through trial and error really complicated kind of funding process in our -- and really diverse. Right?
It was a nice way to have it succinctly but thoroughly kind of explained and assessed, and I think it's everything that we thought it would be and definitely a good thing to have. And I think either in this report or at some point in our talking, we talked about it's something that you'd like to do biennially?

MR. SCOTT: That's correct.

MS. BINGHAM ESCAREÑO: Okay. Very good.

Mr. Irvine?

MR. IRVINE: Tim Irvine, TDHCA staff. I think it's a phenomenally important audit. I think as you exercise your responsibility, there's a tendency to focus so much on the responsibility as it rolls down to the program subrecipients and awardees. But we still have tremendous responsibility to account for the dollars we use ourselves.

And federal funding sources especially and state funding sources, too, look to make sure that, you know, for example, when you're charging salary to a particular grant that you can document and support it. These are the kinds of things for which we ding subrecipients when we go and monitor them, you know. You charged that to CEAP and it shouldn't have been charged to CEAP. Pay us back.

And, you know, to the extent that we are not
keeping these things very carefully properly aligned and
documented, there is repayment risk. So I think it's
something that just really needs a lot of attention and I
think that this is an important part if you’re carrying
out your oversight responsibilities and me carrying out
mine.

MS. BINGHAM ESCAREÑO: Uh-huh.

MR. IRVINE: I also think that in terms of
comfort level when you're dealing with the folks in the
pink building as they go through the appropriations
process and oversee our programs, these are programs that
are extremely hard to understand. It's not simply, Here's
a certain amount of general revenue; go spend it for this
particular purpose.

It's, you know, here are 15 to 20 different
sources of state and federal funds. Use them in an
extremely interwoven and interconnected way to serve
eligible Texans, and that's a very hard story to tell.
And I think an audit like this really helps us to tell
that in an objective and transparent manner.

MS. BINGHAM ESCAREÑO: Yeah.

MR. IRVINE: Thank you.

MS. BINGHAM ESCAREÑO: Thank you. So if there
are no further discussion on Item 2 -- thanks very much --
Mark, we'll move on to Item 3 on the agenda.
MR. SCOTT: Okay, Item 3 is Discussion of Recent Internal Audit and Consulting Activities. On the Audit Plan, I'm in the process of hiring a new auditor to fill a vacancy.

We have two audits in progress that will be presented at the October Audit Committee; those are the Fair Housing Audit and the Compliance Division Audit. The other two audits on the plan, the Federal Tax Credit Audit and the Audit of Multifamily Finance Division, may be carried over into 2017, but I'll try to get them done this year.

Also, at the -- at the upcoming October Audit Committee, I'll present an Audit Plan for approval. The Texas Internal Auditing Act requires a periodic peer review of internal audit, and the internal auditing standards define the period as at least once every five years.

The last peer review of internal audit was completed in January of 2013. The peer review tested Internal Audit Standards 1000 through 2600 all from the Red Book, which is for internal audits. So not only do we do Red Book audits, we also in the past have done Red Book peer reviews.

The Red Book standards apply to internal audits, while the Yellow Book standards apply to external
audits. The Red Book requirement for a peer review is at least once every five years, and we are in compliance with that timeline.

I talked to Tim Irvine about this, and we're going to put the peer review on the Audit Plan in October and also budget for it. And prior to the peer review I will also write up a self-assessment of compliance with Internal Audit Standards 1000 through 2600, which will map to everything in the peer review reports.

On the consulting, I continue to meet regularly with compliance staff to consult on the A-133 audits in accordance with our consulting agreement and with -- and in accordance with the Internal Audit Charter. And that concludes my presentation on the Internal Audit Activities.

MS. BINGHAM ESCAREÑO: Great. Any questions from the committee members --

MR. GANN: No.

MS. BINGHAM ESCAREÑO: -- about the report? So Audit Plan, so you've got a tiny but herculean staff --

MR. SCOTT: Right.

MS. BINGHAM ESCAREÑO: -- that you guys are going to try to knock out everything on the plan this year. But you're letting the committee know that you're short on manpower a little bit and you guys will do the
best you can and keep us posted on status?

    MR. SCOTT: Yes. ma'am, that's correct.

    MS. BINGHAM ESCAREÑO: Okay. And then on peer
review, no questions on peer review. So we're not
actually due -- we're not at our five-year mark yet, but
you guys believe it's something that we can incorporate
into next year, and you'll work with the Executive
Director on that.

    MR. SCOTT: Yes. ma'am, that's correct.

    MS. BINGHAM ESCAREÑO: Great. Mr. Irvine.

    MR. IRVINE: Tim Irvine, TDHCA staff returning
to the microphone. We did receive -- you actually
received, directly to all board members, a letter from
someone outside the Agency raising concerns about whether
we were in compliance with our peer review requirements.

    And I want to be crystal clear and completely
transparent. The instant I learned of that issue, Mark
and general counsel and I immediately went over and just
sat down with our audit manager at SAO and said, Here's
the issue, you know; what do you think, talked it through.

    And I don't think there were any specific
concerns raised, and the general observation was, well,
the best way to address that is get a peer review.

    MS. BINGHAM ESCAREÑO: Right. Uh-huh.

    MR. IRVINE: And there are basically two ways
you can approach a peer review. One, there are members of
various internal audit staffs around agencies, and they
often provide peer reviews for each other.

The problem with that and especially for a
staff that's as slammed as ours is that it's a tit for
tat. If you receive someone else's peer review, then
you've got to contribute your man-hours to go out and do a
peer review.

Also I think that frankly, just from a pure
let's get the maximum benefit from the peer review
process, we would be well served to engage, you know,
somebody that's not in the state auditing world to just
come in and see what they think.

MS. BINGHAM ESCAREÑO: Great. Okay, good.

MR. SCOTT: Yeah, and I'm always open for input
so whatever the peer review says, I'll be open to it.

MR. CHISUM: Tim's conversation raised a
question in my mind about the additional staff.

MR. IRVINE: Yeah.

MR. CHISUM: And our staff is doing a fabulous
job and thank you, Mark. My question is can we -- to get
what you want done in this year, would it be a
consideration to go outside and find the expertise that we
need to help do what you need done to get it done this
year if that's what you want to do?
MR. SCOTT: I mean, I'm open to anything. I don't think that that would necessarily expedite the situation, because we'd have to go through the procurement and all that, and then we'd have to get them up to speed on things that we are learning as we do other audits. We're learning about the audits we're going to do next.

MR. CHISUM: Okay.

MR. SCOTT: For example, we're doing the Compliance Audit and that tells us a lot about Fair Housing, because Compliance tests Fair Housing. So I appreciate the offer, but I don't know if it would necessarily speed things up.

MR. CHISUM: Okay. And then the second part of that question is, okay, that being the case and we go through the process of hiring an additional employee and we've got quite a load -- you do -- to get these things done, once we get those things done, will there be responsibilities remaining for that new employee to continue?

MR. SCOTT: Oh, yes, because, yeah, we'll have to have another audit plan next year.

MR. CHISUM: Okay.

MR. SCOTT: So.

MR. CHISUM: So really we're shorthanded right now that --
MR. SCOTT: That's correct, but we'll work through that.

MR. CHISUM: Okay, thank you.

MS. BINGHAM ESCAREÑO: Thank you, Mr. Chisum.

So -- and then you can do this, we'll probably get together as a committee again in October --

MR. SCOTT: Okay.

MS. BINGHAM ESCAREÑO: -- or somewhere around there. Right? And maybe you'll give us an update at that time on how we're looking to what our -- you know, the completion of our plan and whether or not you think anything will carry over into the coming year.

MR. SCOTT: That's correct. And actually the Internal Audit Act, it says you have to have an annual plan. We do ours based on the fiscal year, but there's nothing that specifies I don't think that you have to do a fiscal year audit plan, and carrying over an audit is never looked at negatively --

MS. BINGHAM ESCAREÑO: Sure. Okay.

MR. SCOTT: -- by the oversight agencies.

MS. BINGHAM ESCAREÑO: Great.

MR. CHISUM: So that being -- Ms. Chairman --

MS. BINGHAM ESCAREÑO: Yes.

MR. CHISUM: That being said then, everything that needs to be done by statute or what other
responsibilities we have for the audits, we'll be able to accomplish that. We're in line with our responsibilities of reporting.

MR. SCOTT: That's correct because the audit -- the Internal Audit Act says you have to prepare an audit plan based on a risk assessment, which we did. You have to conduct the audits, which we did. You have to issue reports on the audit, which we did. We have to report annually on the completion of the audit plan, and then you have to document any deviations from the audit plan.

So in our case we haven't deviated from the audit plan at all, because we haven't taken anything off. We just rolled something forward --

MR. CHISUM: Thank you.

MR. SCOTT: -- so that would put us in compliance.

MR. CHISUM: Good.

MS. BINGHAM ESCAREÑO: Thank you, Mr. Chisum.

MR. CHISUM: Thank you, Ms. Chair.

MS. BINGHAM ESCAREÑO: Thanks, Mark. So Mark, if there's no further discussion on the Internal Audits and Consulting Activity, we'll move on the final item which is the third report item, Discussion of Recent External Audit Activity.

MR. SCOTT: Okay. Yeah, as we've discussed at
several meetings, the external audits of TDHCA are conducted by the SAO and KPMG, and they follow the Yellow Book. The Yellow Book incorporates AICPA standards of testing, statistical sampling, confidence intervals for opining on account balances, opinions on financial statements, et cetera, that don't really apply to internal auditing work.

The SAO is getting ready to start their Financial Statement Audit of TDHCA, which they do every year. And KPMG has finished the field work on their audit of the Energy Assistance Program, and thus far, they've not notified us of any findings.

Also something I report on are the reviews that federal agency monitoring staff do at TDHCA. And these are not technically considered audits, but we do provide them to KPMG and SAO. And HUD just did a review of the Community Development Grant Program and issued a very favorable report.

And that concludes my presentation on external audits, and I'll be happy to answer any questions.

MS. BINGHAM ESCAREÑO: Do committee members have any questions regarding External Audit Activity?

MR. CHISUM: No.

MR. GANN: No, ma'am.

MS. BINGHAM ESCAREÑO: Nor do I. Thank you
very much, Mark.

MR. SCOTT: Thank you.

MR. CHISUM: Thank you, Mark.

MS. BINGHAM ESCAREÑO: Before we adjourn, is there -- are there any additional comments from staff, management, committee?

(No response.)

MS. BINGHAM ESCAREÑO: Great. Then we'll look forward to getting together again sometime around October?

MR. IRVINE: Yes.

MS. BINGHAM ESCAREÑO: Good. Entertain a motion for adjournment.

MR. GANN: So moved.

MR. CHISUM: Second.

MS. BINGHAM ESCAREÑO: All in favor?

(A chorus of ayes.)

MS. BINGHAM ESCAREÑO: Thank you very much. Thank you, guys.

(Whereupon, at 8:23 a.m., the meeting was adjourned.)
CERTIFICATE

MEETING OF:         TDHCA Board Audit Committee
LOCATION:          Austin, Texas
DATE:              July 28, 2016

I do hereby certify that the foregoing pages, numbers 1 through 21, inclusive, are the true, accurate, and complete transcript prepared from the verbal recording made by electronic recording by Nancy H. King before the Teacher Retirement System of Texas.

8/2/2016
(Transcriber) (Date)

On the Record Reporting
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